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CM#116

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

ASSISTANT SECRETARY

AUG 4 1981

MEMORANDUM FOR THE CABINET COUNCIL ON ECONOMIC AFFAIRS

FROM: Marc E. Leland

SUBJECT: International Investment Policy: Report on the CFIUS and the CCEA Working Group on International Investment Policy

There has been a substantial amount of activity in recent months relating to U.S. Government policy on foreign investment. This memorandum reports to the Cabinet Council on Economic Affairs (CCEA) on developments in three areas:

-- the Cabinet Council's Working Group on International Investment Policy;

-- the Committee on Foreign Investment in the United States (CFIUS) review of Elf Aquitaine's takeover of Texasgulf; and

-- suggestions to strengthen the CFIUS.

<u>Working Group on International Investment Policy</u>

The Working Group met for the first time on July 24, 1981, and agreed at that meeting to prepare reports for submission to the CCEA by the end of September, 1981, on two issues:

-- potential problems of foreign government controlled investments in the United States (paper reviewed by the CCEA at July 16, 1981 meeting, see attached list at Tab A); and

-- a survey of national policies and practices relating to foreign investment.

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CFIUS Review of Elf Aquitaine's Takeover of Texasgulf

The CFIUS is continuing to review the takeover. Elf has now acquired approximately 50 percent of Texasgulf's outstanding shares. Elf will control 87 percent of Texasgulf's outstanding shares when the swap with the Canada Development Corporation (CDC) of Texasgulf's Canadian assets (43 percent of the total) for the 37 percent of Texasgulf's shares held by CDC is completed. Two steps are needed to complete the takeover:

-- the swap with the CDC; and

-- the merger of Texasgulf's U.S. assets into Elf.

Both will take some time.

I have prepared a response to French Ambassador de Laboulaye based on the guidance of the CCEA. In summary, the letter makes three points:

-- The CFIUS is continuing its review despite the French Government's decision not to delay. If that review leads to a negative determination, the U.S. Government may take actions to reverse the takeover.

-- The French Government is requested to confirm that any French company with a 5 percent or greater government ownership which is contemplating an investment in the United States should, consult with the CFIUS in advance.

-- The U.S. Government wishes to begin soon bilateral consultations with the Government of France regarding their nationalization and foreign investment policies.

Changes to the CFIUS

Our current problems regarding Canadian investment policies, and the French Government's decision not to intervene in the Elf takeover of Texasgulf, have led to suggestions that the CFIUS should be strengthened. Deputy Secretary of Energy Davis submitted to the CCEA at its last meeting (Thursday, July 30, 1981), a paper for its consideration suggesting that the CFIUS be strengthened and employed by the U.S. Government as a mechanism to retaliate against egregious foreign investment policies (see Tab B). Officials of Texaco Inc. also submitted to the Department of the Treasury a detailed proposal, prepared by their General Counsel, for strengthening the CFIUS (see Tab C). Texaco's target is Canada. Ironically, their model for changing the CFIUS appears to be Canada's Foreign Investment Review Agency (FIRA).

Congressman Rosenthal has also argued in the past, that the CFIUS should be modeled after the FIRA. I'm sure he will repeat that argument at upcoming hearings.

The CCEA needs to evaluate these suggestions to change the CFIUS:

-- A stronger CFIUS would probably be of some benefit in dealing with government controlled investments, such as the Elf take over of Texasgulf. At a minimum, the CCEA might consider imposing stronger requirements and sanctions for advance notification and consultation of this type of investment.

-- On the other hand, any action against private investment could be harmful.

-- Such action might also lead to a negative reaction to our own substantial investments abroad. U.S. investments abroad are almost quadruple foreign investments here, ($193 billion vs. $54 billion). Therefore, the potential liability for the U.S. is much greater.

-- A strengthened CFIUS with powers to restrict private investment would be extremely difficult to control. There could be extreme pressures on the CFIUS from a host of interest groups and the Congress to block foreign investments in the United States.

-- Finally, it's unlikely that retaliation against private foreign investment via a strengthened CFIUS or otherwise would prompt countries to stop their restrictive and discriminatory practices. The Governments of France and Canada, for example, might welcome a restrictive U.S. investment policy that would have the effect of keeping investment capital at home.

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 b A

Listing of Potential Problems Arising From Direct Investment in the United States by Foreign Government Controlled Companies

Competition Policy

-- Government supported circumventions of U.S. antitrust and unfair trade laws. — Justice, USTR, Commerce

-- Foreign government control over selected United States exports/imports. — USTR, Commerce

-- Imposition of rigorous "buy national or home country" requirements on United States subsidiary purchases. — USTR, Commerce

-- Formation of government cartels. — Justice

-- Foreign government manipulation of U.S. production. Foreign operators of the U.S. oil and gas leases may have interests that differ from our own i.e., foreign owners from oil-producing countries might shut in production from U.S. leases to maintain markets for their domestically-produced oil. — Energy, Commerce

-- Foreign government access to information not available to the private business community could give government-controlled firms a distinct advantage. — Justice, Treasury

-- Foreign government control of shares of non-strategic minerals could lead to supply or price pressures if these minerals are exported to the home country or elsewhere. — Interior, Commerce

-- Absolute and/or preferential access to capital not available to private firms. For example are nationalized firms really at arms length with national banks. — Treasury, State

-- High level political intervention and pressure to block or delay Administration of U.S. antitrust and unfair trade laws. — USTR, State, Treasury

National Security

-- Investment in downstream energy production (refinery operations) may upset Defense security of supply. — Defense / Energy

-- Investment in U.S. corporations under contract to produce weapons or equipment for the Department of Defense. — Defense

-- Investments in sole-source or few-source suppliers of intermediate or of raw goods to defense industries (strategic minerals). — Defense / Interior

-- Flexibility of operations under crisis or sub-crisis environments. — Defense

-- Strict control of subsidiary operations (e.g. technology, product development, growth) could have national security implications; particularly industries such as specialized synthetic fuels, chemicals, high technology sectors, minerals extraction and processing. — Defense / Commerce / State

-- Extensive control by foreign concerns of U.S. energy service and distribution systems could create special regional security problems, i.e., localized control of gas stations or terminals. — Defense / Energy / Commerce

Tax Policy

-- Policy implications if a foreign government seeks to resolve a tax dispute at a high level bypassing normal channels. — Treasury

-- Possible difficulty in obtaining books and records of foreign parent. — Treasury

-- Negotiation of competent authority settlements in double taxation cases. — Treasury

-- Freedom from taxation of dividends in certain circumstances. Treasury

-- Foreign governments have access to information, available under mutual assistance provisions of tax treaties, which include pricing and other economic data concerning the U.S. competitors of the domestic corporation which it controls. Treasury

-- Difficulty in obtaining data for U.S. tax purposes under mutual assistance provision when foreign corporations controlled by foreign government. Treasury

Disclosure

-- There may be difficulty in obtaining information where such information is held by non-controlled affiliates of the foreign investor or by unrelated foreign entities rather than by the entity required to make a pre-merger filing. Such entities may be beyond U.S. jurisdictional reach. Justice / SEC

-- Problems in discovery by antitrust suit or actions under foreign corrupt practices act or anti-boycott legislation. Justice

Some other problems of disclosure are given in the tax and competition sections.

Political and Legal

-- Difficulty of United States residents suing foreign government-controlled U.S. subsidiaries. Justice

-- Normal legal action by the U.S. federal or state government may trigger action against U.S. investment abroad. USTR / Comme / State

-- Linkage of political, diplomatic, or military issues with economic issues relating to foreign government-controlled subsidiaries. Treas / State / USTR / Comme

-- High level political intervention to influence U.S. legal actions against foreign government owned subsidiary in the U.S.	Treasury State USTR Commerce
-- Possible use of corporate power to influence U.S. policy.	Treasury Commerce

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Declassification on 7/14/87

Tab B

29 July 1981

Comments made at the last Cabinet Trade Policy Committee meeting underscored the problems inherent in depending on existing legislative authority to target U.S. retaliation to the investment policies of offending nations. We need to seek new legislation to overcome these problems and while the legislative process plays out, we need to take steps which signal our concerns. A strengthened Committee on Foreign Investment in the U.S. (CFIUS) could be the vehicle through which we achieve these two objectives.

CFIUS could take immediate steps to review proposed mergers of a foreign investor with a U.S. company on a case by case basis and recommend actions to the President based on current legislative authority. Such reviews could be initiated by CFIUS, by a Federal agency or by a petition from U.S. industry. CFIUS should be expanded to ensure that the total applicable federal expertise is incorporated during these reviews.

Without additional legislation, CFIUS recommendations would be limited but if we launch and announce this step now we would clearly signal our concerns to offending nations. I suggest you give full consideration to assigning CFIUS the task of developing operating procedures and an announcement to activate this proposal.

In addition, CFIUS, which possesses considerable experience and will be gaining more as the new role evolves, should be assigned the task of developing proposed legislation that will provide us the flexibility we need to have the option to target U.S. retaliation to the investment policies of offending nations. Consistent with this, the Mineral Leasing Act of 1920 should be ammended to provide for a flexible response. If Congress provides new authority, the legislative limits on CFIUS could then be removed. Full consideration could then be given to our foreign policy, national security and evonomic concerns before we decide on a course of action. I suggest you give full consideration to assigning this role to CFIUS and to announcing it at an appropriate time.

An increased role for CFIUS could provide a flexible tool that presents a real barrier to foreign investments detrimental to the U.S. and yet would preclude the ramifications of moratoriums which have been proposed in Congress. I look forward to seeing your reactions.

A PROPOSAL FOR A UNITED STATES GOVERNMENT INITIATIVE ON FOREIGN INVESTMENT

It has been proposed that consideration be given by the U.S. Government to the use of the Committee on Foreign Investment in the U.S. (CFIUS) as a means for obtaining modification of Canadian discriminatory energy and investment policies. It was suggested that a new Executive Order be issued expanding and restructuring CFIUS responsibilities and authorities to include the following:

- Foreign investment in U.S. companies of all types, above a threshold level in terms of percent equity or asset value, would be candidates for review, particularly those from countries where "national treatment" of foreign investment is not available to U.S. investors. Prior notice of a proposed investment, accompanied by relevant information, would be filed with CFIUS. No transaction would be completed prior to a CFIUS review, and public offerings for listed stocks would not be permitted prior to release of the review "findings".

- Criteria for CFIUS review would include a positive finding of benefit to the U.S. economy, not simply the absence of a negative impact, and reciprocal treatment of U.S. investment by the country from which the foreign investment comes.

- Public notice in the Federal Register of the pending review and subsequently of the conclusions of the review would be required. Parties at interest would be permitted to file comments and participate in the proceedings as appropriate.

- Findings by CFIUS would be taken into consideration by the SEC, FTC and Department of Justice in their separate reviews.

- Representation on CFIUS would be elevated to higher level officials of the concerned Departments as evidence of increasing U.S. concern over the foreign investment issue.

- A specific time period for completion of the review would be established, for instance 60 to 90 days.

- Data and information requirements concerning foreign investments would be comprehensive and detailed.

Attached is a research paper relating suggestions for strengthening CFIUS to the relevant sections of the Foreign Investment Act of 1974.

7/21/81

REGULATION OF FOREIGN INVESTMENT IN THE UNITED STATES AUTHORIZED BY THE FOREIGN INVESTMENT STUDY ACT OF 1974

1. Prior notice to CFIUS of proposed investment accompanied by relevant information.

   5(2) and (3) direct Secretary of Commerce to "survey the reasons foreign firms are undertaking direct investment in the U.S." and "the processes and mechanisms through which foreign direct investment flows into the U.S."

   6(1) gives Secretary of Treasury authority to investigate scope of foreign portfolio investment in U.S.

   7(6) gives Secretaries authority to promulgate rules to carry out functions under Act. These rules could delay proposed investment until study completed, otherwise purposes of study would be frustrated.

2. No investment completed prior to CFIUS review.

   7(c) prevents Secretaries from divulging information submitted to them under 7(b) or using it except for analytical or statistical purposes. However, this limitation applies only to information submitted by foreign investor, not to information gathered by experts or submitted at public hearings.

   CFIUS could advise SEC and FTC, and Department of Justice of findings. FTC and Department of Justice could seek court order enjoining anticompetitive investment.

3. Public offerings for listed stocks delayed until CFIUS findings issued.

   7(b) authorizes Secretaries to require all persons subject to U.S. jurisdiction (this would include foreign investors in U.S.) to maintain records and furnish relevant information. However, that authority has expired and must be renewed by legislation.

   SEC has authority to delay by stop order the effectiveness of any registration if registration statement contains any untrue statement of a material fact or omits to state a material fact. SEC should determine that a necessary element in determining whether a registration statement is accurate is findings contained in CFIUS study and that if result of study is unfavorable the result must be disclosed in prospectus.

4. No foreign investment permitted without positive benefit to U.S. economy.

Underlying basis of study is that extensive foreign investment might be harmful to national economy, but that absent adequate data no assessment of impact could be made. If study reveals dramatic increase in foreign investment without benefit to U.S. economy, legislation would be recommended to halt foreign investment - purpose of study, according to House Report No. 93-1183 is to "help lay the foundation for a national policy concerning foreign investments in the U.S."

5. No foreign investment permitted without reciprocal treatment of U.S. investments in country from which investment comes.

6(7) directs Secretary of Treasury to compare U.S. laws on foreign portfolio investment with laws of other nations and 6(8) directs him to compare treatment of U.S. investors abroad with U.S. treatment of foreign investors.

6. Public notice of pending review;
7. Public notice of conclusions of review;
8. Public comment permitted

4 directs securing information from industry and other groups. A logical and efficient way to gather information is to hold public hearings on specific proposed foreign investments, and to publicize results of study.

5(3) directs Secretary of Commerce to determine the effects of foreign financing methods on American financial markets. Again, best way to make determination is to gather information at public hearings and through written submissions from the public.

9(a) authorizes Secretaries to hire experts and consultants.

9. SEC, FTC and DOJ to consider CFIUS findings in reviewing foreign acquisitions.

<u>SEC</u>

Legislative history (House Report No. 93-1183) indicates that "the subject being studied covers matters that fall under the jurisdiction of other governmental agencies, such as, ...portfolio investment-Securities and Exchange Commission."

5(11) directs Secretary of Commerce to study adequacy of information, disclosure and reporting requirements and procedures.
5(4) directs Secretary of Commerce to determine scope and significance of foreign direct investment in acquisitions and takeovers of existing American enterprises.

Both of these topics are within jurisdiction of SEC and should be considered by them in assessing transactions.

FTC and DOJ

5(4) directs Secretary of Commerce to determine effects of direct investment on domestic business competition. Both of these agencies would be derelict in not considering findings of CFIUS in discharging their duties, particularly if anti-competitive effect found.

House Report anticipates that "the Departments of Commerce and Treasury should consult extensively with the appropriate governmental agencies and departments in both the construction of the survey ... and in the analysis of the data."

10. High level membership or CFIUS.

2 directs Secretary of Treasury and Secretary of Commerce to conduct study. Although they are permitted to delegate authority, they need not do so.

11. Review completed in specific time period.

10 An interim report was to be submitted by CFIUS by October 1975 and a full report was due April 1976. Since Committee is not abolished upon completion of initial study, President could direct them to undertake additional study to be completed within a specified time.

12. CFIUS to compile comprehensive and detailed data.

2 Secretaries of Treasury and Commerce "authorized and directed to conduct a comprehensive, overall study of foreign direct and portfolio investments in the United States".